

**Opening Statement of Stephen P. Fox
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**FTC/DOJ Hearings on Competition and Intellectual Property
Law and Policy in the Knowledge-Based Economy**

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Introduction

Hewlett-Packard applauds this FTC/DOJ initiative to explore critical issues at the intersection of intellectual property and competition law and policy. We welcome the opportunity to offer our perspectives, particularly some thoughts on how your agencies can contribute to the evolution of patent and antitrust law regimes in directions that encourage innovation activity.

The innovation focus of these hearings goes to the heart of the history of our company from roots in a garage 63 years ago to its present day pioneering role in enterprise computing, printing and imaging, information technology services and infrastructure solutions. The “Invent” logo attached to our name speaks volumes about both the driving force behind our success in the past several decades and the central imperative to continued success in the years ahead. We take large risks in our investments in R&D across a broad range of complex technologies. Risk is inherent in all of our markets in light of the array of rivals we confront, rivalry from both established firms with comparable R&D resources and aggressive upstarts with new ideas that can literally change the world tomorrow.

Both the patent and antitrust law regimes critically influence our risk-taking and risk management policies. Both regimes in their current iterations create combinations of incentives and disincentives to our investment in R&D activity. Both regimes could be materially improved in ways that serve the public interest in maximizing innovation and technology development generally.

1. **The Patent Law Regime**

HP relies on the patent law regime to enable us to realize return on investments in innovation efforts. We seek patent protection for our inventions both to prevent rivals from free-riding on our investments and to counter or minimize exposure to other firms' blocking patents and hold-up strategies. Our patent portfolio enables us to pursue a variety of policies to protect our inventions, from appropriately aggressive prosecution of infringing uses to licensing and cross-licensing arrangements that remove patent clouds and ensure design freedom for further initiatives.

The current state of the patent law system is problematic from HP's standpoint. We have witnessed in recent years a vast proliferation of patent grants by a seriously understaffed PTO and an equally vast proliferation of complex litigation over patent validity and scope. Notwithstanding the centralization of patent law development in the Federal Circuit over the past two decades, the governing standards for patentability and patent law jurisprudence generally remain plagued by unpredictability in their application, particularly with respect to patents bearing on new or emerging technologies. The result is pervasive uncertainty about legal rights, both in terms of ability to enforce one's own patents and ability to avoid rapidly escalating exposures to infringement claims by others. And that uncertainty heightens risks surrounding innovation investment decisions.

Those risks, moreover, are a growing menace to innovation efforts across the information technology landscape. Given how much they burden and impair a company as resourceful as HP, the loss to society from their cumulative impact on companies large and small including the most otherwise promising start-ups unable to raise capital for their projects in this environment must be considerable. It is without doubt a serious drag on the technological and scientific progress that the patent system was designed to promote.

Competition policy is deeply implicated in this unsatisfactory situation. An unknown but undoubtedly significant number of invalid patents are issued; an unknown but undoubtedly significant

number of patents generate lawsuits or threatened lawsuits involving overbroad claims. Both phenomena create serious impediments to competition, both from existing products on the market and from new products in the development stage. Litigation has become a poor means of addressing these problems, in part because of the unacceptably high cost and length of the litigation process and in part because of the already mentioned unpredictability of litigation outcomes. There are high stakes for plaintiffs and defendants alike in these suits. There are, however, equally high unrepresented stakes for the public in these same suits. Courts are called upon to adjudicate sharply conflicting arguments over IP rights without hearing from a voice on behalf of the public's interest in results consistent with innovation-encouraging competitive markets.

We would respectfully suggest a new role for the Federal Trade Commission and the Department of Justice in filling that gap. Specifically, both agencies could look for appropriate cases in which they would participate in an amicus capacity to present their perspectives on issues of patent law with significant competition policy implications. There are many issues of this sort on which the Federal Circuit in particular could benefit from FTC or DOJ input. Examples of issues on which the Federal Circuit could benefit from your agencies' thoughtful analysis of competitive effects include all of the following: (i) patent claim certainty versus the doctrine of equivalents; (ii) licensee estoppel; (iii) when patent misuse should and should not coincide with antitrust liability, (iv) prosecution latches or late claiming; and (v) the proper role of juries in patent cases.

2. **The Antitrust Law Regime**

In his address discussing the plans for these hearings last November, Chairman Muris emphasized the fundamental consistency between intellectual property and antitrust law in their

objectives of promoting innovation and enhancing consumer welfare.¹ HP fully endorses that view and welcomes the interest of the antitrust agencies in advancing the development of both law regimes with those consistent objectives in mind.

There have nonetheless been points of conflict between these regimes. From HP's standpoint, the conflicts of consequence in recent years have come less from FTC or DOJ initiatives than from the ease with which private parties can prosecute treble-damage antitrust claims improperly implicating IP rights. The problem has been compounded by a lack of sufficient guidance available to generalist judges in their rulings on motions to dismiss or for summary judgment in such cases. One way in which these FTC/DOJ hearings could be useful in this regard would be by shining light on the issues of most concern and thereafter supporting various forms of guidance from the agencies to courts for their use in the adjudication of private suits.

The agencies' 1995 "Antitrust Guidelines for the Licensing of Intellectual Property" were well-received by both antitrust and IP counselors to high technology companies such as ours, particularly among those of us with enough gray hair to remember the notorious "Nine No-No's" era of the 1970s. Over the seven years since the 1995 promulgation, however, there has been considerable controversy over a range of issues either unaddressed or inadequately addressed therein. These issues could appropriately become the focus for either updated guidelines or other means of disseminating guidance based on these hearings (including through reports or speeches by agency officials in the months ahead). Permit me to offer some thoughts now on one such issue that has been the subject of extensive private litigation in recent years: antitrust attacks on unilateral refusals to license IP rights.

In 1997, the Ninth Circuit affirmed a treble-damage judgment against Kodak for what the opinion characterized as a unilateral refusal to sell patented parts and to license copyrighted materials to

¹ "Competition and Intellectual Property Policy: The Way Ahead," Prepared Remarks of FTC Chairman Timothy J. Muris Before ABA Antitrust Section Fall Forum, November 15, 2001, at 2 (hereafter "Muris Remarks").

competing independent service organizations.² The court adopted a “rebuttable presumption” that a patent or copyright owner’s refusal to license was supported by the owner’s legitimate interest in exclusive control over its own property. It then, however, held that the jury in the case before it was justified in finding Kodak’s refusal to be unlawful “exclusionary” conduct based on entirely subjective evidence of “anticompetitive” intent. Three years later, the Federal Circuit upheld Xerox’s virtually identical refusal to license its patents and copyrighted materials to its service competitors in affirming a district court’s grant of summary judgment in Xerox’s favor.³ The Federal Circuit flatly rejected the Ninth Circuit’s rebuttable presumption rule as applied to patents while adopting a variation of it that excludes subjective evidence as applied to copyrights. For unilateral refusals to license patents, the court in essence adopted a rule of per se legality:

In the absence of any indication of illegal tying, fraud in the Patent and Trademark Office, or sham litigation, the patent holder may enforce the statutory right to exclude others from making, using, or selling the claimed invention free from liability under the antitrust laws.⁴

As Chairman Muris noted in his November address, there are diverse views about the Xerox decision, and its effect has been more rather than less debate over whether or when refusals to license can be a basis for antitrust liability.⁵ Xerox is also not the last word from an appeals court in this general area. In June of last year the D.C. Circuit in its decision in the Microsoft case flatly rejected Microsoft’s intellectual property defense of challenged provisions in its Windows licenses to OEMs.⁶ As the court noted:

² *Image Technical Services v. Eastman Kodak Co.*, 125 F.3d 1195 (9th Cir. 1997).

³ *In re Independent Service Organizations Antitrust Litigation*, 203 F.3d 1322 (Fed. Cir. 2000).

⁴ *Id.* at 1327.

⁵ Muris Remarks at 6-7.

⁶ *United States v. Microsoft Corp.*, 253 F.3d (D.C. Cir. 2001) (*en banc*).

The company claims an absolute and unfettered right to use its intellectual property as it wishes: “[I]f intellectual property rights have been lawfully acquired,” it says, then “their subsequent exercise cannot give rise to antitrust liability.” Appellant’s Opening Br. at 105. That is no more correct than the proposition that use of one’s personal property, such as a baseball bat, cannot give rise to tort liability. As the Federal Circuit succinctly stated: “Intellectual property rights do not confer a privilege to violate the antitrust laws” [quoting from the Xerox decision].⁷

HP believes the Federal Circuit was exactly right in its holding that a unilateral refusal to license IP rights cannot by itself constitute the conduct element of an antitrust violation. And, as applied to refusals to license patents, that holding should now be considered a binding precedent across the country under the Federal Circuit’s national jurisdiction over antitrust issues in patent cases. At the same time, HP accepts what might now be called the D.C. Circuit’s “Baseball Bat Doctrine”: IP licensors are not free to bludgeon their licensees into accepting anticompetitive license conditions without scrutiny under the antitrust laws. That said, however, there are disagreements over the scope and application of both of these points, and lack of clarity on the positions of the enforcement agencies on them. One example of a highly controversial license condition now being employed in the context of software *copyright* licensing is a broad constraint upon licensees’ assertions of present or future *patent* rights against the licensor or other licensees that are frequently horizontal competitors. In HP’s view, these provisions are anticompetitive insofar as they diminish future innovation incentives and innovation rivalry. We would in any event welcome meaningful agency guidance on their legality.

More generally speaking, uncertainty over IP owners’ freedom to decide when to license or not license their rights and uncertainty over conditions they may appropriately impose in their license agreements invite litigation and impede efforts to develop and commercialize new technologies. The

⁷ *Id.* at 63.

FTC and DOJ could usefully clarify standards in these areas in the aftermath of these hearings. Doing so could advance public policies at the core of both the IP and antitrust laws.

There are other subjects at the intersection of the IP and antitrust law regimes that should also be addressed in these hearings and should then become candidates for thoughtful agency guidance. Areas of particular interest to HP include licensing practices of patent pools and IP policies implemented in standard-setting processes. My HP colleagues, Jeff Fromm and Scott Peterson, will discuss these areas in some detail in their appearance at the April segment of these hearings. I will take just a few moments to outline our general perspectives on them.

(a) **Patent Pools**

Patent pools have become critically important mechanisms for enabling widespread use of new technologies that require access to a multitude of patents dispersed among a multitude of parties. Combining all “essential” patents into single “package” licenses openly available on reasonable terms to all interested parties can promote innovation and competition generally throughout new markets. The DOJ’s Business Review Letters on the MPEG-2 and DVD pools have provided valuable guidance on how to structure these arrangements in a manner that avoids antitrust exposure. The problem from our standpoint is undue rigidity in how participants in the patent pool world interpret and apply the advice in those letters with regard to the terms of package license offers.

The common approach today is a “one-size-fits-all” license for the totality of patents within the pool. But a new entrant seeking access to the technology in question at some point after the pool has been formed may only need a fraction of all of the covered patents since it may already have access to many of them through existing licenses or cross-licenses with several pool participants. Or the new entrant may not be interested in implementing the entire standard. Applicants in these situations should be able to license the set of patents they need without being forced to take and pay for the whole package. Forcing upon them what in their case is a combination of needed and completely unneeded

licenses raises entry costs and thereby impedes competition. (They may, for example, end up paying twice for many of the patents being bundled together.) The proffered alternative of individual negotiations with pool participants holding patents that the new entrant needs is often impractical for many reasons, including patent holders' lack of incentives to accommodate the interests of the new entrants.

We are highly skeptical about claims that offering partial licenses would be "inefficient." There surely is room for choice and flexibility in license terms. In our view the agencies should expressly encourage evolution of these pool structures in this unambiguously procompetitive direction.

(b) **Standard-Setting**

HP is an active participant in a wide array of standard-setting processes critical to the development of innovation-encouraging and competition-encouraging information technology infrastructures. We constantly confront the need to consider incorporation of proprietary intellectual property, particularly patents or technology subject to patent applications, into specifications intended to become standards that will be open to all comers on a level playing field. As Chairman Muris aptly observed in his November address, "[s]tandards that rely on intellectual property can raise difficult competition issues,"⁸ and these issues are the subject of intense debate within many of the groups in which HP participates.

The FTC's Dell Computer action of six years ago called attention to the manner in which anticompetitive "patent hold-up" or "patent ambush" situations can arise when standard-setting bodies go about their business of fashioning standards and voting upon them without knowledge of the patent implications of the standards they adopt. That action, however, opened a virtual Pandora's Box of follow on issues over how to address and minimize exposure to post-adoption opportunistic conduct by

⁸ Muris Remarks at 8.

holders of patents required for a standard's use. There is no single essential solution appropriate for the myriad of standard-setting contexts. Different groups are now employing or considering different approaches, involving a variety of pre-adoption patent disclosure and license commitment policies. There is no appropriate "one-size-fits-all" in this realm. Everyone concerned about these issues, including your agencies, should welcome this diversity of experience and of experimentation with methods of addressing recognized problems.

That said, however, HP has in some circumstances favored an approach that we believe should be encouraged but that is often opposed by others upon what we believe is a misapprehension of antitrust risks. If a party promoting use of its patented technology for incorporation in a proposed standard states it is willing to offer a license on terms that are "reasonable and nondiscriminatory" (but terms not otherwise specified), consideration of the impact of the patent on the proposed standard often ends at that point -- indeed some participants insist any further or more specific discussion about it would invite antitrust trouble. All potentially affected parties have a legitimate interest in knowing before standards decisions are made what the economic effects will be of accepting a patent into the standard. Yet, when suggesting that the impact of patent licensing terms be considered, we have encountered the objection that disclosure of particular licensing terms could be attacked as unlawful "price-fixing." That objection is in our view wholly unfounded. To the contrary, disclosures of the sort we have suggested would be procompetitive by foreclosing opportunistic hold-up situations that are all too easy to arise when a patent holder's view of "reasonable" license terms remains secret until after a standard has been adopted. This is an area where the agencies could constructively clarify their view of permissible and desirable disclosure practices.

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Finally, with regard to all of the issues I have discussed and all others affecting the IP-competition policy interface, it is important to keep in mind the interconnected impact of law and policy

regimes throughout the world but particularly between the United States and the European Union. Conflicts or inconsistencies in applicable principles among jurisdictions impede innovation and technology development generally. HP believes that your agencies could play an important role in promoting international harmonization of IP rights in the same manner that you have so persistently promoted harmonization of competition policy on a global basis.

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Let me conclude by reiterating HP's appreciation for the care and thoughtfulness with which these hearings have been organized. We support and encourage followup initiatives that provide enlightened guidance to courts and affected business communities on critically important issues at the intersection between the intellectual property and antitrust law regimes.